DOLLARIZATION AND DUAL CURRENCY
ISSUES AND RECOMMENDATIONS

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The dual currency regime is characterized by high level of dollarization;

Effective monetary policy by the Central Bank of Liberia (CBL) is difficult;

The US dollar share of broad money remains high: 71.3 percent at end-May, 2016;
DOLLARIZATION AND ITS IMPACTS

- **Dollarization** - the departure from holding of portfolio in domestic currency to foreign currency.

- **Major forms:**
  - **Transaction dollarization** or currency substitution, which is the use of the dollar as a means of payment in domestic transactions.
  - **Financial dollarization**, the substitution of local currency assets or liabilities for those in foreign currency.

- **Reduces exchange rate risk** by reducing exchange rate friction between currencies;

- **Makes the supply of liquidity** costly due to seigniorage loss;

- **Creates weak control** over monetary and exchange rate policy;

- **Exposes** the economy to external shocks, etc.;

- **May encourage Capital flight**
DEPOSITS: US & LIBERIAN DOLLARS AND DOLLARIZATION RATIO

- Over **80 percent** of deposits are denominated in US dollars.
- Deposits dollarization on average was **86.3 percent** from March, 2007 to December, 2012.
- The high level of dollarization is partly due to high public confidence in the US dollar.

SOURCE: CENTRAL BANK OF LIBERIA
Credit to private sector denominated in US dollar on average was 95.0 percent from March, 2007 to March, 2016;

A maximum of 97 percent and minimum of 91 percent, signaling the high level of dollarization in the country;

Businesses and consumers are comfortable in taking US dollar denominated credits due to the stability in its value.
An economy is dollarized if the ratio of foreign currency deposits to broad money exceeds 30 percent (Baliño, Bennett, and Borenstein, 1999);

Liberia in 2015 was the 2nd most dollarized economy amongst selected developing countries;

In selected WAMZ countries Liberia and Ghana were the two dollarized countries at end-2015;

Liberia dollarization ratio was 70.2 percent in 2015, from 61.0 percent in 2007;

Ghana dollarization ratio was 33.3 percent in 2015, from 20.9 percent in 2007.

Amongst the countries selected, Liberia is the only country with dual currency regime while Cambodia, the most dollarized country, has multiple currency regime.
It is important to note that the use of a single currency does not guarantee stable exchange rate as shown in the graph;

In order for the domestic currency to appreciate, there is a need for real sector diversification (agriculture, manufacturing etc.) that adopts a value added growth model.
The Central Bank of Liberia believes it is only prudent to move to a single currency through collaboration with fiscal authorities and consultation with the Economic Management Team Chaired by H.E Madam President.

In order to achieve De-dollarization, a gradual market approach begins with 1) Transactional De-dollarization followed by 2) Financial De-dollarization.

There is a need to develop a road-map that will guide the process of De-dollarization.
THANK YOU!